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california | **City of Glendale**
Finance
Internal Audit

141 N. Glendale Ave., Room 346
Glendale, CA 91206-4975
Tel 818.551.3020
www.glendaleca.gov

July 23, 2015   REPORT #: 2016-01

Robert Elliot, Director
Finance Department

Dear Bob,

Enclosed is the final audit report for the Disbursements and Duplicate Payments Audit. Internal Audit would like to thank you and your staff for the support and assistance provided to us during the audit.

Should you have any questions, please feel free to contact Natalie Minami-Valdivia or myself.

Thank you,

Eileen Donahue,
Internal Audit Manager

Enclosure

CC: Yasmin Beers, Assistant City Manager
      Afshin Bokaei, Purchasing Manager
      Lily Fang, Finance Administrator
      Michele Flynn, Assistant Director of Finance
      Christine Maldonado, Accounts Payable Supervisor
      Michelle Nguyen, Fiscal Operations Manager
      Scott Ochoa, City Manager
      City Council
      Audit Committee

Disbursements and Duplicate Payments Audit

July 23, 2015

Background

In accordance with Internal Audit's fiscal year 2014-15 audit plan and at the request of the Finance Department, Internal Audit performed an audit of the City of Glendale's (City's) disbursements and duplicate payments.

City disbursements for department operations are processed through the central financial accounting system, PeopleSoft, by the Finance Department's Accounts Payable Section in accordance with City policies and procedures.

At the time of our fieldwork the Accounts Payable Section consisted of an Accounts Payable Supervisor, two Accounts Payable Technician I's, and an hourly City worker.

Disbursements result from the purchase of goods or services. The three standard methods used to make purchases are contracts, purchase orders and request for demands (RFDs). Both a contract and purchase order establish an obligation with a vendor before the goods or services are received while a RFD is used solely for the payment of invoices for directly purchased goods and is limited in aggregate to $15,000 per vendor, per department, per fiscal year. Any RFD in excess of $15,000 requires approval by the City Manager.

Departments are responsible for reviewing the accuracy of vendor invoices and obtaining proper approvals before forwarding invoices to the Accounts Payable Section for processing.

Duplicate payments occur when a vendor is paid more than once for a specific service or goods. To prevent duplicate payments from processing, PeopleSoft has a control to systematically detect transactions for identical vendor number, invoice number, invoice date, and amount.

Objective, Scope and Methodology

The objectives of this audit were to determine that disbursements were made in accordance with governing policies and procedures and duplicate payments were prevented.

Our audit covered the period July 1, 2013 through June 30, 2014 with approximately 39,000 disbursements totaling $556 million processed through the Accounts Payable Section.

In order to accomplish the audit objectives, Internal Audit performed the following:

- Obtained and reviewed purchasing and accounts payable requirements from the City's Administrative Policy Manual.

- Obtained and reviewed portions of the Accounts Payable Accounting Procedures.

- Conducted interviews with key Finance purchasing and accounts payable personnel.

- Performed a walk-through of the vendor set-up process and invoice payment process.

- Evaluated user access rights for vendor entry and

approval and voucher/invoice entry access rights.

- Analyzed disbursement data using Arbutus audit software and data analytic techniques for specific attributes such as gap analysis, vendor-employee address matching, off-cycle checks, Benford's Law (first digit) analysis, split payment, rounded invoices, duplicates, and employee-single payment comparison.

- Segregated the disbursement universe and analyzed data in order to make an informed selection of individual disbursements to test for aggregate payment criteria for compliance with policies and procedures.

- Judgmentally selected 104 disbursements by vendor each in excess of $15,000 (individually or in aggregate) with a sum total of almost $7 million to test for payment limit attributes with appropriate approvals.

Summary of Results

We obtained an understanding of the requirements necessary to support a valid disbursement and the review procedures conducted by the accounts payable staff before a transaction is allowed to process through PeopleSoft for payment.

We found that the Accounts Payable Section has a thorough process of reviewing documentation submitted by departments for disbursements. Additionally it was noted that in FY 2013-14 the Accounts Payable Section returned over 2,000 invoices to departments requesting added information before processing the payment.

We learned that PeopleSoft systematically detects and prevents duplicate payments. In FY 2013-14, approximately 500 invoices totaling $2.2 million in duplicate payments were prevented from processing. However through our analytic test work we identified eight duplicates outside the PeopleSoft systematic controls that allowed for a duplicate disbursement to the vendor totaling $529,000.

We performed extensive analytical test work on disbursements through the use of audit software and found no significant anomalies. In addition, we analyzed invoice amounts and aggregate payments to vendors to ensure compliance with payment limits of the City's purchasing policies and procedures.

Through our detailed analysis we found that the majority of aggregate payments to vendors in excess of $15,000 are in compliance with the payment limit requirements of the City's policies and procedures. However, there were a few areas where exceptions to the City's policies have been allowed for certain entities and transactions. As well, the individual test work found that there is no monitoring or enforcement for compliance of the RFD aggregate payment limit up to $15,000 per vendor, per department, per fiscal year. Thus, 33 vendors were identified with aggregate payments in excess of the $15,000 limit totaling over $815,000 of which two vendors received aggregate payments greater than $50,000.

Conclusion

Overall, we found that the City disbursements analyzed for the period July 1, 2013 through June 30, 2014 generally follow the required City policies and procedures for payment limits by vendor and duplicate payments are significantly limited by a systematic means.

Through the results of our test work we identified seven issues for improvement which are summarized by risk rating in the chart that follows and included in the Observation, Recommendation, and Management Response Section of this report.

| **Priority 1** |
| Critical control weakness that exposes the City to a high degree of combined risks. |

- o Incompatible PeopleSoft user access.
- o Shortcomings of vendor file maintenance.
- o Undocumented payment situations.

| **Priority 2** |
| Less than critical control weakness that exposes the City to a moderate degree of combined risks. |

- o Some Policies and Procedures of the Administrative Manual are outdated.
- o RFDs by vendor aggregated in excess of $15,000 are not monitored for policy compliance.
- o Duplicate payments not systematically detected for invoices with different dates.

| **Priority 3** |
| Opportunity for good or better practice for improved efficiency or reduce exposure to combined risks. |

- o Tracking of payment submission flaws not communicated regularly to departments.

Item	Observation	Recommendation	Management Response
Priority 1 1.	Based upon review during fieldwork of the PeopleSoft user access rights for vendor entry/approval and invoice entry, we noted the following: • Due to staffing limitations, two individuals within the Accounts Payable Section were granted the ability to perform the incompatible duties of establishing a vendor, approving the establishment of the vendor, inactivating the vendor, posting vouchers, overriding match requirements, comparing electronic fund transfer changes to the appropriate supporting documentation, and running a payment cycle. • Three individuals in the Finance Department, Accounting Section were provided the access rights to enter invoices however the function is no longer necessary. • One individual in the City Attorney's Office with the ability to enter vendors no longer requires the access for the position.	It is recommended that the Finance Department perform the following to strengthen controls: • In the situations where individuals are allowed access rights that are defined as incompatible, additional mitigating controls should be designed and implemented to reduce the risk of errors or irregularities; examples of some mitigating controls to consider include independent monitoring, exception reports and random transaction reviews. • Establish a procedure whereby the PeopleSoft user access listing is reviewed and updated at least annually limiting access to the minimum possible and remove access no longer necessary.	Finance management agrees with the recommendation and recognizes that ideally individuals authorized to update the vendor file should not be authorized to process payments or enter purchase orders. However, at this time because of current business processes and staffing constraints, it is not feasible to separate these functions. As we implement a new financial system over the next two to three years, business processes along with user access will be fully evaluated. In the meantime, we will periodically review the vendor audit report for appropriateness. We reviewed the listing of names provided to Internal Audit for user access to vendor maintenance and invoice processing and have made changes which included requesting to eliminate access for individuals who no longer need it. A full review of PeopleSoft user access will take place once the current report of access is received from ISD and then at the beginning of each fiscal year after that. The anticipated completion date is September 30, 2015.

Item	Observation	Recommendation	Management Response
Priority 1	2. Based upon discussions with the Accounts Payable Supervisor and the Purchasing Manager, we noted the following shortcomings in controls regarding vendor set-up/maintenance: • No periodic review of vendor maintenance edit reports is currently performed. • Vendor master file is not reviewed on an annual basis to inactivate stale vendors. • No standardized form is used to document the vendor set-up process. Select individuals in some departments other than Finance have been granted vendor set-up access and supporting documentation for those records are not centrally located.	It is recommended that Finance management implement the following to strengthen controls over vendor records: • Develop a procedure to perform an independent review of the vendor maintenance file edit report on a periodic basis. • Implement a procedure to review for inactive stale vendors. • Implement use of a standard vendor set-up form and secure centralized database for retrieval of documents that support the vendor set-up records. Alternatively, Finance management could consider whether operations support the creation of a dedicated position separate from Purchasing and Accounts Payable that focuses solely on vendor set up including vendor authentication for all City departments.	Finance management agrees with the recommendation and a vendor audit report will be reviewed periodically for reasonableness. In addition, inactive vendors will be deactivated as appropriate. The first of these reviews will be completed by September 30, 2015. Vendors are set-up in the Finance Department, Worker's Compensation section of Human Resources, and the Housing section of Community Development. Each area maintains documents responsible for their vendors. Similar to the response in #1 on the previous page, the possible centralization of vendor set-up, maintenance of records, and a vendor set-up form will be visited as business processes are reviewed during the new financial system implementation.

Item	Observation	Recommendation	Management Response
Priority 1	3. Although no misuse of funds or inappropriate activities was identified it was noted that Accounts Payable Section processes some payments that fall outside of the City's purchasing policies. The criteria for these situations are not documented as to proper form, support and approvals. The areas noted were for certain entities and/or for particular payment types as follows: • Verdugo Job Center-tuition reimbursement/on-the-job training • Refunds • Rebates • Glendale Redevelopment Agency-share of operating expenses/façade improvement reimbursement • Interagency Communications Interoperability System-UPS and antenna installation • Affordable Housing-loan proceeds • Benefit related vendor fees • Certificates of Participation (COP's) purchaser's counsel fees • Investment consulting fees	It is recommended that Finance management evaluate the payment situations that do not follow the requirements of the City's purchasing policies to ensure the level of authorization and support provided for payment processing is adequate to ensure payment requests are not inappropriate. Further the treatment of these payments and required support and approvals should be documented, approved through the City Manager's Office, and communicated to personnel processing payments.	Finance management agrees with the recommendation and after discussions with staff, has determined that the payment situations noted that do not follow the requirements of the City's purchasing policy are appropriate and we agree they require clarification within the current policy. These situations will be summarized and documented as an addendum to the existing policy once approvals are obtained from the City Manager and City Attorney's offices. The anticipated completion date is December 31, 2015.

Item	Observation	Recommendation	Management Response
Priority 2 4.	Some policies and procedures of the City's Administrative Policy Manual suggested for audit criteria were found to be outdated as follows: • The Accounts Payable Administrative Policy Manual has not been updated since January 1, 1997. As such, changes from updates to the Purchasing Administrative Policy, current practices and internal procedures are not reflected which provides necessary guidance to department staff in the submission of their payables. • Administrative Policy 3-20 for Software Lifecycle is outdated and does not align with current practices for software maintenance procurement and required purchase approvals.	The following is recommended for the Finance Department: • Review and update the Accounts Payable Administrative Policies and Procedures to reflect current policy and practice. • Communicate with Information Services Department (ISD) management to discuss procurement and purchase approval expectations for software maintenance to ensure the Accounts Payable staff are accurately informed of criteria to support a software maintenance disbursement. Further communications should include discussion on either revising or eliminating the Software Lifecycle Policy.	Finance management agrees with the recommendation. The Accounts Payable policy is currently in draft and will be finalized and implemented by December 31, 2015. After the current ISD Director was recruited and when the Purchasing Policy was implemented, a decision was agreed-upon between Purchasing, ISD and the City Manager that software would be purchased according to the new Purchasing Policy causing this portion of the Software Lifecycle Policy to be superseded. Finance will communicate this finding to ISD.

	Item	Observation	Recommendation	Management Response
Priority 2	5.	Given results of the examination of disbursements aggregated by vendor we noted that departments are not monitoring for the requirement of limiting RFDs in aggregate to $15,000 per vendor, per department, per fiscal year. As such approval through the City Manager's Office is often not obtained before submittal for payment, there is a potential that purchases by RFD may circumvent the standard procurement process when the vendor aggregate is allowed to exceed the RFD payment limit.	It is recommended that the Finance Department continue to work with ISD to finalize and make available to the departments a report of all payments to vendors on request for demands by total per department, per fiscal year to actively monitor the aggregate payments.\n\nFurther, additional approval conditions through the City Manager's Office should be required in the policies and procedures for disbursements to vendors that exceed the $15,000 aggregate limit by fiscal year.\n\nVendors that are identified with RFD disbursements in excess of the annual payment limit should be evaluated for an alternative method of purchase such as by purchase order or contract.	Finance management agrees with the recommendation. A report has been created but needs to be finalized and approved for implementation. The report will provide information to all departments on the vendors they are utilizing that are close to exceeding the authorized $15,000 per fiscal year limit. It's anticipated that a report will be available for distribution by December 31, 2015.\n\nAn exception clause was not originally approved for implementation in the existing Purchasing policy. This clause would indicate that approval from the City Manager's office must be obtained prior to processing payments not in accordance with the policy. However, this approval is obtained on all exceptions currently. Finance will re-visit an exception clause for the Purchasing policy with the City Manager and the City Attorney by December 31, 2015.\n\nWhen discovered, alternative purchase methods are discussed immediately with departments. This takes place on a continuous basis.

	Item	Observation	Recommendation	Management Response
Priority 2	6.	Based upon our analytical test work, we identified duplicate payments that occurred outside of the PeopleSoft systematic prevention process as follows: • Six duplicate payments totaling $2,974 in overpayments as the result of different invoice dates, but same invoice numbers and amount. • Two duplicate payments, totaling almost $526,000 were made to a health insurance vendor that submitted dual invoices with the same invoice date and amount but different invoice numbers. Fortunately the vendor applied the additional payment to future costs and efforts were taken by City employees to research the situation. Further, we noted that for one vendor individual invoice numbers were not entered in PeopleSoft due to the volume; rather the statement number was used which does not allow for duplicate payment detection through PeopleSoft.	It is recommended that the Finance Department perform the following: • As resources allow review the payment file for duplicate payments based on payments with matching vendors, invoice numbers, and gross amounts. • Ensure refunds have been obtained from the vendors where overpayments occurred and continue to allot time to research unexpected large credits. • Reference individual invoice numbers on statements entered to enable the departments to review for prior payments and for operation of the PeopleSoft control. As a means to track payments and establish an annual payment limit, establish a purchase order for the estimated costs of the City's annual health insurance premiums.	Finance management agrees with the recommendation. System controls allow for Accounts Payable to stop the processing of the vast majority of duplicate invoices submitted for payment. To the extent resources are available, staff will review the system data for further duplicate payments. Effective July 1, 2015, the Accounts Payable Section is requesting departments to submit individual invoices for vendor payment rather than statements. All duplicate payments identified have been researched. Resolutions include the application of $526,420 in credits to subsequent medical premium invoices, receipt of $1,744 in reimbursements, and a stop payment on an outstanding $147 duplicate payment. Efforts are being taken to apply the $620 duplicate payment of an annual professional membership to future year membership fees for department employees. We will further evaluate establishing annual purchase orders for health insurance premiums.

	Item	Observation	Recommendation	Management Response
Priority 3	7.	Department personnel responsible for submitting and approving payment requests are not regularly notified by the Accounts Payable Section on the level of returned invoice activity for added information or the prevented duplicate payments to actively make changes in the control processes for review and approval.	It is recommended that the Finance Department communicate regularly with the departments on the returned invoices and duplicate payments as a means to reiterate to the departments all payment requests and supporting documentation should be reviewed for completeness, previous payment, and accuracy before submittal to the Accounts Payable Section.	Finance management agrees with the recommendation. A log of all duplicate payment requests and returned items is maintained by Accounts Payable staff. We will discuss the distribution of this information with the City Manager's office by August 15, 2015 and begin distributing the log immediately upon approval.